



**IT IS ORDERED as set forth below:**

**Date: June 27, 2007**

**Paul W. Bonapfel  
U.S. Bankruptcy Court Judge**

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE NORTHERN DISTRICT OF GEORGIA  
ROME DIVISION**

IN RE:	:	Case Nos 04-40656 through
	:	04-40658
Southwest Recreational Industries, Inc., et al.	:	
	:	Jointly Administered Under
Debtor.	:	Case No. 04-40656
	:	
	:	
Ronald L. Glass, as Chapter 7 Trustee of Southwest	:	
Recreational Industries, Inc.,	:	
Plaintiff,	:	
vs.	:	Adv. No. 05-4066
	:	
Isotec International, Inc.,	:	
Defendant.	:	
	:	

**ORDER ON MOTIONS FOR SUMMARY JUDGMENT AND ON  
DEFENDANT'S MOTION TO STRIKE OR, IN THE ALTERNATIVE, DISMISS**

Within the 90 days preceding the filing of its chapter 11 bankruptcy case on February 13, 2004, Southwest Recreational Industries, Inc. (the "Debtor") made three payments totaling

\$96,215 to one of its suppliers, Isotec International, Inc. (“Isotec”). Ronald L. Glass, as the chapter 7 trustee for the Debtor following the conversion of its case to chapter 7 (the “Trustee”), filed this adversary proceeding to recover the payments as avoidable transfers under 11 U.S.C. § 547(b).<sup>1</sup>

Both parties have moved for summary judgment. The parties agree that the Trustee has established all of the elements of a preference under § 547(b) but dispute whether Isotec is entitled to the ordinary course of business defense of § 547(c)(2). Under § 547(g), Isotec bears the burden of establishing the defense. *E.g., Miller v. Florida Mining and Materials (In re A.W. & Associates, Inc.)*, 136 F.3d 1439, 1441 (11<sup>th</sup> Cir. 1998). While Isotec asserts that its evidence shows that it has done so as a matter of law, the Trustee insists that Isotec has failed to demonstrate the existence of a material fact to be tried.

Isotec also moved to strike the Trustee’s motion for summary judgment as untimely filed. For reasons stated at the hearing held in this matter on February 20, 2007, the Court will deny the motion to strike and consider the Trustee’s motion for summary judgment as well as Isotec’s.

As applicable here prior to its amendment by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, the ordinary course of business defense to a bankruptcy trustee’s preference action in § 547(c)(2) requires the creditor to prove three elements. First, the creditor must prove that the transfer was “in payment of a debt incurred by the debtor in the ordinary course of business or financial affairs of the debtor and the transferee.” § 547(c)(2)(A).

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<sup>1</sup>This Court has authority to hear and determine this proceeding under 28 U.S.C. § 157(b)(1) as a core proceeding under 28 U.S.C. § 157(b)(2)(F) within the District Court’s jurisdiction under 28 U.S.C. § 1334(b) that the District Court has referred under 28 U.S.C. § 157(a) and L.R. 83.7, N.D.Ga.

Second, the creditor must prove that the transfer was made in the ordinary course of business or financial affairs of the debtor and the transferee. § 547(c)(2)(B). Finally, the creditor must show that the transfer was made “according to ordinary business terms.” § 547(c)(2)(C). The dispute here concerns the latter two provisions.

The Congressional purpose of the ordinary course of business defense in § 547(c)(2) is to protect “those payments which do not result from ‘unusual’ debt collection or payment practices.” *Marathon Oil Co. v. Flatau (In re Craig Oil Co.)*, 785 F.2d 1563, 1566 (11<sup>th</sup> Cir. 1986). In determining whether transfers occurred in the ordinary course of business of the debtor and the transferee within the meaning of § 547(c)(2)(B), “the issue is whether the transfers in question were made in a similar manner to transfers made prior to the preference period. The factor to focus upon is whether the payment(s) were made in response to unusual debt collection or payment practices.” *Scroggins v. BP Exploration & Oil, Inc. (In re Brown Transport Truckload, Inc.)*, 161 B.R. 735, 739-40 (Bankr. N.D. Ga. 1993).

“Lateness is particularly relevant in determining whether payments should be protected by the ordinary course of business exception,” *Craig Oil Co.*, 785 F.2d at 1567, but late payments are considered ordinary if the transferee shows that late payments were the normal course of business between the parties. *E.g., Ellenberg v. Plaid Enterprises, Inc. (In re T.B. Home Sewing Enterprises, Inc.)*, 173 B.R. 790, 795-96 (Bankr. N.D. Ga. 1993). In this regard, the transferee must establish a “‘baseline of dealings’ so that the court may compare the practice of late payments during the preference period with the prior course of dealing.” *Id.* at 795.

In addition to satisfying the subjective test under § 547(c)(2)(B) that the payments were in the ordinary course of business between the parties, the transferee must also meet the objective

test of § 547(c)(2)(C) that the payments were made “according to ordinary business terms.” “ ‘[O]rdinary business terms’ refers to the *range* of terms that encompasses the practices in which firms similar in some general way to the creditor in question engage, and that only dealings so idiosyncratic as to fall outside that broad range should be deemed extraordinary and therefore outside the scope of subsection C.” *Miller v. Florida Mining and Materials (In re A.W. & Associates, Inc.)*, 136 F.3d 1439, 1443 (11<sup>th</sup> Cir. 1998) (*quoting In re Tolona Pizza Prods. Corp.*, 3 F.3d 1029, 1033 (7th Cir.1993)) (emphasis in original).

The debtor made the three transfers here by check. The first check for \$87,240, dated December 5, 2003, paid five invoices, two dated September 11, 2003, one dated September 12, and two dated September 16. The second check for \$1,659, dated December 22, 2005, paid a single invoice dated September 11, 2003. The third check for \$7,316, dated January 30, 2004, paid a single invoice dated October 24, 2003. (Exhibit A to Affidavit of Michael Fuqua, Exhibit 1 to Plaintiff’s Statement of Material Facts [Doc. 17, pp. 5, 9]). Isotec contends that the three payments were made, respectively, on December 15 and 26, 2003, and February 6, 2006. (Paragraph 6 of Affidavits of Charles Knight and William McNiff, attached as Exhibits A and B to “Notice of Filing Discovery Materials” [Doc. 19, pp. 3, 4; 20, 21]).

The parties have presented their theories with regard to the timing of the payments by reference to the time between the invoice date and the date of payment. The Trustee’s analysis of the payment history between the debtor and Isotec is set forth in the “Supplemental Affidavit of Michael Fuqua” (“Fuqua Supp. Aff.”). (Exhibit B to Plaintiff’s Response to Defendant’s Statement of Facts [Doc. 26, p. 21]). Mr. Fuqua is an employee of the Trustee’s accounting firm who analyzed payment history based on information supplied by Isotec for the period from

November 3, 2000 to February 6, 2004. (Fuqua Supp. Aff. ¶ 1,2, 3, 7). He concludes that the range for the number of days between invoice date and payment date range from 29 days to 145 days. He notes that the longer end of the range is only 97 days if one transaction on the records is a non-cash offset rather than a payment. (Fuqua Supp. Aff. ¶ 7).

Because many payments covered several invoices of differing dates (like the first payment at issue here), Mr. Fuqua analyzed the payment history in three ways. First, he calculated the times between the date of each invoice and the date of the applicable payment. (Fuqua Supp. Aff. ¶ 10). Second, he calculated the times between the date of the oldest invoice in a group and the date of payment for all of them. (*Id.* ¶ 11). Third, he calculated the times between the date of the newest invoice in a group and the date of payment for all of them. (*Id.* ¶ 12). In each circumstance, he calculated the average number of days between invoice date and payment date and the percentage of payments that occurred between 31 and 70 days from the date of invoice. The calculations are as follows (*Id.* ¶¶ 10-12):

<u>Method – Time between:</u>	<u>Average</u>	<u>% Between 31-70 days</u>
Each invoice and its payment	54 days	88 %
Oldest invoice in group and payment	64 days	71%
Newest invoice in group and payment	49 days	95%

Based on this analysis, Mr. Fuqua concludes that the “typical practice” for the four year period preceding the preference period was that payments would be made between 31 and 70 days after the invoice date because this was true, under the three analyses, for 71% to 95% of all payments. (*Id.* ¶ 13-14).

Because the three payments in question here were made 90 days or more after the invoice

dates, the Trustee concludes that they were not made in the ordinary course of business between the Debtor and Isotec and that they were not made according to ordinary business terms.

Isotec does not dispute the facts assembled by Mr. Fuqua or his arithmetic calculations but asserts that the analysis “does not demonstrate the true business and payment relationship of the parties.” (Defendant’s Brief in Support of Supplemental Consideration at 3 [Doc. 32, pp. 16, 18]). Isotec relies on affidavits of two of its officers and one of the Debtor’s to support its contentions that the payments were made consistently with the payment pattern and ordinary course of business history between the Debtor and Isotec and that the payments were within industry standards.

Charles Knight is Isotec’s President and Chief Executive Officer and has been in the chemical supply industry for 40 years. (Affidavit of Charles Knight (“Knight Aff.”) ¶¶ 2, 27, attached as Exhibit A to Defendant’s Notice of Filing Discovery Materials [Doc. 19, 3, 27]). Mr. Knight states that the Debtor and Isotec had a relationship for the purchase and sale of chemical products from November 3, 2000 to February 6, 2004. Mr. Knight asserts that “Debtor and [Isotec] had an established relationship, and as a consistent large orderer of product Debtor was given deference on invoice payments in consideration of the established relationship and consistency and amount of orders.” (Knight Aff. ¶¶ 8-9). He further states:

10. Industry standards for unestablished relationships is to consider an invoice late after payment is not made after 90 days, with acceptance of payments late when an established consistent relationship is in place and when invoices are grouped in payment. Debtor’s payment [sic] were in accordance with industry standard, and the established relationship of [Isotec] and Debtor allowed for

payments on invoices to be grouped together in payment and paid within the range of up to 145 days.

11. Industry standards in the chemical supply industry show that payments of 90 days or over on invoices are acceptable and normal in an established [sic] due to the payment structure and timing of the debtor's ability to pay and consistency of orders. The ordinary business terms between Debtor and [Isotec] consisted of payments of invoices grouped together and paid at once, sometimes resulting in invoices being paid upon or after 90 days after due to being paid with other invoices in one payment. [Isotec] and Debtor established this normal course and business practice at the beginning and in duration of its relationship.

26. [A] majority of payments on [the Debtor's] invoices were paid in excess of 60 days, with a number of them over 80 days. [The Debtor] routinely waited and paid several invoices at once.

27. I have been in the chemical supply industry for 40 years. It is industry standard, particularly in the chemical supply industry, to expect and accept payments on invoices during a 90 day period from date of invoice, and often longer when it is an established customer with frequent and consistent orders. This occurs because typically you are selling to middle-men suppliers or installers who have to wait on their payment before [Isotec] is paid.

William McNiff, Isotec's comptroller who has been in the chemical supply industry for ten years and a comptroller in charge of supply accounts for 25 years, confirms Mr. Knight's

statements. (Affidavit of William McNiff (“McNiff Aff.”), attached as Exhibit B to Defendant’s Notice of Filing Discovery Materials [Doc. 19, p. 20]). Mr. McNiff adds that “a consistent and established relationship results in leniency and accepted group payments of invoices due to how the supplied party is getting paid.” (McNiff Aff. ¶ 27).

Isotec has also submitted the affidavit of Kevin Swank, a former vice president of the Debtor. (Affidavit of Kevin Swank (“Swank Aff.”), attached as Exhibit A to “Motion of Supplemental Consideration” [Doc. 32]). Mr. Swank generally confirms the views of Mr. Knight and McNiff with regard to the relationship, and adds some additional information. Thus, Mr. Swank states (Swank Aff. ¶ 10, 12, 16):

10. Industry standards in the chemical supply industry show that payments of 90 days or over on invoices are acceptable and normal due to the payment structure and timing of the debtor’s ability to pay, and the established relationship of [Isotec] with Debtor and circumstances of middle-man supplier payments allowed for payments on invoices to be grouped together in payment and paid within the range of up to 145 days. The ordinary business terms between Debtor and [Isotec] consisted of payments of invoices grouped together and paid at once, sometimes resulting in invoices being paid upon or after 90 days after due to being paid with other invoices together in one payment. [Isotec] and Debtor established this normal course and business practice at the beginning and in duration of its relationship.

12. The subject Transfers parallel payment patterns on other previous invoices between [Isotec] and Debtor in time and amount. The Transfers



identified by Plaintiff were made by [Debtor] to [Isotec] consistent with the inconsistent payment and payment pattern of past invoices, and payment made earlier in some instances.

16. During the business relationship period, due to our established relationship, Isotec would and did allow [Debtor] extensions on invoices up to 145 days to pay due to project circumstances or supplier issues.

Mr. Swank's affidavit discusses certain circumstances relating to delays in payment due to problems on various projects (Swank Aff. ¶ 17) and states that payments owed to Isotec had to be delayed until issues were resolved and the Debtor received payments. (*Id.* ¶ 18). Although it is not clear from the affidavit whether the specific circumstances relate to the payments in question here, Mr. Swank states that the subject payments "were a result of issues with supplier payments, as had occurred in the past during the relationship with Isotec, and were certainly in the course of good and acceptable practices between Isotec and SRI." (*Id.* ¶ 19).

With regard to industry standards, Mr. Swank states (Swank Aff. ¶ 21):

It is industry standards, particularly in the chemical supply industry, to expect and accept payments on invoices during a 90 day period from date of invoice, and often longer when it is an established customer with frequent and consistent orders and routine delays due to unavoidable supplier issues. This occurs because typically you are selling to middle-men suppliers or installers who have to wait on their payment before [Isotec] is paid.

The Trustee's evidence with regard to the lateness of payments, unrebutted or unexplained, would be sufficient to establish the absence of an ordinary course of business

defense under § 547(c)(2). Although the Trustee has thus “pierced the pleadings,” Isotec’s evidence, viewed in its favor, is sufficient to establish the existence of genuine disputes of material fact that must be tried. From Isotec’s evidence, the Court could find that the payments qualify as being in the ordinary course of business dealings between the Debtor and Isotec, as § 547(c)(2)(B) requires, because they were not made in response to unusual collection activities or payment practices. Although they were made later than most of the payments during the “baseline” period, this fact alone does not establish that they were not in the ordinary course of business. Viewing the evidence in Isotec’s favor, the Court could find that the payments were made consistently with a business relationship between the parties that permitted the deferral of payment until the resolution of issues relating to jobs for which the chemicals were ordered.

Similarly, Isotec’s evidence, viewed favorably to it, could permit the court to find that the payments occurred according to ordinary business terms as § 547(c)(2)(C) requires. If the Court finds Mr. Knight and Mr. McNiff to be credible and knowledgeable – determinations that the Court cannot make in considering motions for summary judgment, the Court could find that the payment practices were within the broad range of practices in which similar firms engage and that they were not so idiosyncratic as to fall outside that range. Contrary to the Trustee’s argument, expert opinion evidence is not required to prove the ordinary business terms element. *See Webster v. Fujitsu Consulting, Inc. (In re NETtel Corp.)*, 2007 WL 1541493, \* 10 (Bankr. D.D.C. May 22, 2007).

But if the Court viewed Isotec’s evidence favorably to the Trustee, the Court could make contrary determinations. The lateness of the payments is a critical circumstance that undermines Isotec’s position on both issues. Thus, Isotec’s evidence does not clearly and definitively

establish its positions as a matter of law.

The Court cannot conclude, as a matter of law, that the record establishes that Isotec has or has not proved the factual issues that are essential to its ordinary course of business defense under §547(c)(2). Accordingly, the motions of both parties on these issues must be denied.

Based on the foregoing, it is hereby **ORDERED and ADJUDGED** as follows:

1. Isotec's Motion to Strike, or in the Alternative, to Dismiss, is denied.

2. The Trustee's motion for summary judgment is granted in part. The Trustee has established, as a matter of law, that the three transfers the Debtor made to Isotec were preferential transfers within the meaning of § 547(b), and is entitled to partial summary judgment on those issues. The Trustee's motion for summary judgment is otherwise denied.

3. Isotec's motion for summary judgment is denied.

4. The Court will hold a telephonic status conference with regard to this matter at 10:00 o'clock a.m. on July 11, 2007 to discuss the preparation and submission of a proposed pre-trial order, the scheduling of trial on the remaining issues, and any other matters that may be appropriate with regard to this matter. Counsel are directed to contact the Courtroom Deputy Clerk, Ms. Cheryl Goss, 404-215-1021, and to provide a telephone number at which counsel may be reached at that time.

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